RESPONSES OF THE ELECTRICITY CONSUMERS RESOURCE COUNCIL TO CONGRESSMAN DINGELL'S APRIL 10, 1997 QUESTIONS

May 16, 1997

Question 1: Some proponents of retail competition hold the view that all electricity resources should be sold at a market price and that state authority to regulate retail rates should be eliminated. Do you agree with this statement or not, and why?

ELCON Response:

No. Those products and services, such as generation, which lend themselves to competition, should be priced exclusively in the marketplace. Other services such as metering, customer billing, and energy management should also be "unbundled" and offered on a competitive basis at market-determined prices. However, services such as transmission, distribution, and system operation should continue to be regulated as natural monopolies, by federal and state regulators, as appropriate[1]. Transmission and distributions owners may only offer the services for the use of those facilities under rates subject to economic regulation, *i.e.*, at rates based on cost of service plus a reasonable opportunity to earn a fair return on all prudently incurred investments that remain used and useful.

Certainly, the most significant change being proposed is the deregulation of generation markets. Congress partially deregulated this market in 1978 with the enactment of Title II of the Public Utility Regulatory Policies Act (PURPA), which guaranteed market access to certain qualifying facilities. In recent years, half of all new generating capacity in the United States has been added by independent producers. Since the enactment of Title VII of the Energy Policy Act of 1992, which established another category of independent producers ("exempt wholesale generators" or EWGs) and required FERC to implement rules for open-access in wholesale electricity markets, increasingly competitive wholesale electricity markets have emerged in most regions of the country. This trend has been facilitated by a fast-growing new breed of suppliers, the power marketers. Their intermediary role in these markets has tremendously added

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[1]Interstate transmission and distribution services, and system operation for maintaining the reliability of the interstate interconnections, should be FERC jurisdictional. States retain jurisdiction of intrastate distribution and operation of intrastate distribution for reliability purposes. Privately-owned transmission and distribution facilities would continue to be allowed and not be subject to state or federal jurisdiction.

to market liquidity -- a necessary prerequisite for true competition. Market conditions and technologies now make it possible for the next step -- full retail access to generation markets -- to be implemented.

Question 2: ***In states in which retail competition is adopted, who do you believe should get the benefit of generation resources which currently produce power at below market cost? Should shareholders or ratepayers who historically have been served by such resources retain the benefits, and if so how should the benefits be apportioned among these parties? Alternatively, should the power from such facilities simply be sold to the highest bidder? Do you believe there should be any "transition" rules to govern the interim and soften the adjustment period for these parties? What about shareholders' interests?***

ELCON Response:

Most of the concern in the restructuring debate is who bears the burden of high-cost generation and power purchase agreements. If it is public policy to make customers pay for stranded ("above-market") generation costs, then customers should be the beneficiaries of "below-market" generation.[2] Customers should not be responsible for all above-market costs, at the same time shareholders are the sole beneficiaries of below-market costs. The two issues must be dealt with consistently.

ELCON advocates the sharing of the burden of above-market costs and assets, and therefore, the benefits of below-market costs should similarly be shared. Many utilities will have a combination of such assets, in which case, one should be used to offset the other. Any utility that has greater below-market assets than above-market should share those benefits with its existing customers. Establishing a price cap is one such mechanism for capturing those benefits. This would have the effect of a "negative" competition transition charge (or CTC).[3] This process would be determined by each jurisdictional state regulatory body and apply during a transition period to full competition.

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[2]A strict application of this policy would, in essence, defer the onset of real competition and its benefits until all generation costs are equilibrated.

[3]The CTC is the mechanism originally proposed in California for recovering above-market, "stranded" costs from customers. The CTC would be a line item charge on every customer's bill which would be separate and independent from the charges billed for their basic electricity services.

However, restructuring the electricity industry is not a zero-sum game, *i.e.*, not simply a reallocation of existing resources. Customers who would forego the other benefits of competition to preserve access -- or entitlement -- to existing low-cost resources may not be acting in their own best long-term interests. In addition to lower cost products and services, competition offers greater innovation, and new and better products and services. Customers must balance their desire to retain access to today's lowest cost resource, without unduly sacrificing future new benefits. After all, the operation of even today's lowest cost utility generators can be improved.

Question 3: In hearings before the Energy and Power Subcommittee during the last Congress, some witnesses took the position that Congressional legislation mandating retail competition is necessary to protect the interests of small and residential consumers. This was based on the assertion that large industrial customers are able to negotiate lower rates with state utility commissions, and the incidence of such rate reductions is on the increase.

a. Do you agree with these observations?

b. Are you aware of any study or analysis that would confirm or refute these assertions?

c. What is ELCON's experience with respect to the historical relationship between residential and industrial rates, the extent to which one customer class has subsidized another, and whether this trend has altered in recent years?

ELCON Response:

The answer to subquestion (a) is yes because we believe the only way all small consumers in every state will be guaranteed the opportunity to benefit from customer choice is by a federal mandate. In states like Michigan, total cost savings can be substantial and produce significant across-the-board economic benefits. A recent economic study shows that rate reductions of 20% or more would produce total savings of over $1 billion per year.[4] This would be a tremendous stimulus to the Michigan economy.

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[4]Strategic Energy Ltd. *Competitive Options for Michigan Power Users,* Sponsored by the Association of Businesses Advocating Tariff Equity, October 1995. The one-page executive summary from this study is attached.

But even industrial customers do not now have choice, except for the option to self-generate or the few who participate in state authorized pilot programs. To the extent that many states are unwilling to restructure their power sectors without a federal mandate, such legislation will also benefit industrial consumers.

Many large industrial customers have been able to "negotiate lower rates" for several reasons, all of which are legitimate and nondiscriminatory, and have been common practice since the beginning of the industry. The existence of these negotiated rates or special contracts does not mean that these customers are not paying their fair share of the cost of service. In all cases, the negotiated rate merely brings rates closer to the utility's actual cost of service. In many cases, the negotiated rate remains in excess of true cost of service.

Large customers have such options because:

(1) The state government requires it, usually to promote economic development.
(2) Large industrial consumers are typically served under contracts, not rate tariffs. Contracts allow for "give and take" between the customer and suppliers, the terms of which must be periodically renegotiated.
(3) Many industrials can generate their own electricity or exercise other options.
(4) Utilities are trying to retain their largest customers and the utilities' regulators have sanctioned such efforts.
(5) Federal law encourages the use of cogeneration.

The perception that negotiated, non-tariff rates harm small customers is unfounded.[5] In most such cases, the utility's other customers would have been harmed more had the industrial customer not received the lower rate and had left the system altogether, and thus, not contribute to any costs. The only instances where other customers are made technically worse off, is when industrial customers are no longer required to subsidize other, primarily, residential customers. As a pre-condition to negotiated, non-tariff rates, state regulators typically prohibit any cost shifts to remaining customers. For example, the Michigan Public Service Commission has put its jurisdictional utilities on notice that they will have a very heavy burden of proof if they seek any realignment of costs in future rate case proceedings as a result of their new contracts with large customers.

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[5]It is also alleged that these options are being used to escape so-called "stranded costs." No state that is now implementing or committed to implementing customer choice is absolving any customer class from this responsibility -- where it has been determined that it is a consumer responsibility. Industrials will pay their share; their concern is that they will pay more than their fair share.

The utility's other customers are not harmed by negotiated contracts as long as the industrial customer's alternative costs (*e.g.*, to cogenerate) are higher than the utility's marginal cost to provide the service, provided that the alternative option would result in the industrial customer leaving the system. Each contract negotiated between the industrial customer and its utility is subject to state commission approval to ensure that other customers are no worse off as a result of the contract. The typical rate paid by an industrial customer under these contracts is not solely based on the utility's short-run variable costs (fuel plus losses), but also includes a contribution to fixed costs.

The lost revenues associated with each new contract, compared to what the customer would have paid under the old contract, are usually absorbed by the utility until the next rate case proceeding, unless a prior proceeding established an alternative cost recovery mechanism. Usually, the utility and its shareholders pick up the difference. In recent years, many utilities have cut their costs (or were the beneficiary of lower costs, such as fuel costs) and these savings effectively offset the lower revenue stream resulting from the negotiated contracts. When and if a new rate case proceeding is initiated, these and other cost allocation adjustments are reviewed together. This may include the reduction or elimination of cross-class subsidies. This is discussed in greater detail below.

Non-Tariff Supply Arrangements

Many large electricity consumers take service from their utilities under contracts rather than under a published tariff. Depending on the state or utility, each contract can be customized. In recent years, the contract terms are relatively short, often only a couple of years before each has to be renewed. Industrial customers increasingly sought shorter-term contracts in order not to foreclose any new opportunities that may arise as the industry changes. Utilities, on the other hand, were looking for greater load security by attempting to lock their largest customers into longer-term contracts. Some utilities have offered such customers a lower rate (and sometimes for a *lower level of service*) in return for a longer-term contract. This preserves the large customer's load on the system, contributing to load diversity, and thus a more economical load factor, and earnings stability.

In Michigan, the focus of these contracts is not so much the "Big Three," but the hundreds of manufacturers that supply parts to the automobile companies. As the auto companies have been successful in outsourcing parts, competition among parts suppliers has increased. This has forced many companies to shift production to states where costs are lower, if those costs cannot be made more competitive in Michigan.

On-Site Generation and Other Options

Many, but not all, large customers have limited opportunities to self-generate or cogenerate electricity, to switch fuels, assist the local town or city with municipalization, shift production to more economical facilities, or exercise other legal and prudent business practices that result in lower-cost electricity service. It should be self-evident that the economic viability of such options is in direct proportion to the utility's costs. This is a risk that utilities have always faced during the industry's hundred-year history.[6] In situations where a utility (and its regulators) believe that the potential to bypass was legitimate, the utility (and its regulators) often approved a lower rate based on the economics of the customer's alternative supply.

Elimination of Cross-Class Subsidies

Finally, since the 1970s, there have been many efforts to distort rate design from a cost-of-service basis in an attempt to promote certain social objectives. Tail block rates[7] were deliberately increased to force price elastic customers to reduce their consumption of electricity, ostensibly, with energy conservation. Those rate designs were often based on erroneous or misconceived assumptions about future fuel prices and generation costs. Higher tail block rates also made many utility-sponsored conservation programs artificially cost effective relative to a more realistic cost-based tail block rate and in essence, created the basis for the indirect subsidization of those programs.

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[6]During the industry's early history, most large customers generated their own electricity. In 1900, self-generation (called "isolated plants") accounted for 60% of total U.S. capacity. This made sense to the large customer because, by self-generating, they did not incur any system costs associated with transmission and distribution, which to them, made the utility's rates based on total costs too high. Only by offering them a lower rate -- but nonetheless at least equal to the utility's short-run marginal costs -- did large customers switch to the utility. By 1973, self-generation accounted for only 4.2% of total capacity.

[7]Traditionally, the most common rate design for electricity service was the "declining block" rate. Each rate had two or three components: (1) capacity or demand charges, (2) energy charges, and (3) customer costs. The demand charge and customer costs (also called "fixed charges") did not change based on the amount of energy the customer consumed. These charges were collected up front with the first block(s) of usage. Subsequent energy charges would decline as usage increase. The last block of usage (called the "tail" block) might be a charge for energy based on the utility's incremental fuel costs, plus losses. For example: a customer might be charged $10.00 per month for the first 50 kWh or less of usage; 10¢ per kWh for the next 50 kWh; 7¢ for the next 100 kWh; and 5¢ for all usage over 200 kWh.

At the same time, many utilities were completing the construction of very high-cost power plants (mostly nuclear). In order to avoid potential "rate shock" on residential consumers, state regulators over-allocated the fixed costs of these plants to industrial customers. In effect, the initial blocks of residential rates were reduced in order to subsidize these customers.

ELCON commissioned the first survey on this issue in 1977. Based on utility cost-of-service studies, the survey demonstrated that cross-subsidization was by then widely practiced. That survey was subsequently updated and expanded in 1978 and 1982. The 1982 survey was the most comprehensive and used data on 100 utilities, with some data going back to 1968. The survey found that industrial customers were subsidizing residential customers in 94 out of 100 utilities surveyed. In only 6 cases was there evidence of residential customers subsidizing industrial customers. What the data also showed was a situation getting worse.[8] As a utility's capital costs increased, industrial customers were forced to pay an increasingly disproportionate share of those costs.

In 1986, ELCON conducted another survey to determine the dollar amount of the subsidies on an industry-wide basis. That survey showed that industrial customers paid more than $2.5 billion (or $3.6 billion in 1995 dollars) annually in subsidies to other ratepayers. In 1988, residential customers of Consumers Power Company received subsidies totalling over $103 million; this increased to $114 million in 1991.[9] In 1990, residential customer on the Commonwealth Edison system received subsidies totalling over $188 million.[10] It should be obvious that for over two decades industrial (and other non-residential) customers have been forced to pay a disproportionate share of the fixed costs associated with what are now deemed utilities' "stranded costs."

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[8]The U.S. economy at that time was generally a mess; created, in part, by the so-called "energy crisis." Interest rates and inflation were high, and utilities were having an increasingly difficult time financing their future stranded costs.

[9]These numbers are based on the company's own cost-of-service studies which may, in fact, understate the magnitude of the actual level of subsidization. Nicholas Phillips, Jr., *On Behalf of the Association of Businesses Advocating Tariff Equity (ABATE),* Michigan Public Service Commission, Case Nos. U-9346 (*In the Matter of the Proceeding, on the Commission's Own Motion, to Examine the Electric Rates of Consumers Power Company*) and U-9346 (*In the Matter of the Complaint of the Association of Businesses Advocating Tariff Equity Against Consumers Power Company with Respect to its Electric Rates*), June 1990.

[10]Maurice Brubaker, *Testimony and Exhibits on Behalf of the Illinois Industrial Energy Consumers,* Volume 1, Illinois Commerce Commission, Docket No. 90-0169, August 1990.

Each of these practices -- the elimination of cost-based declining block rates and the imposition of cross-class subsidization -- ignored real cost responsibility and the fact that many large customers always retained the option to self-generate or exercise other options to obtain more cost-effective service.[11] In recent years, in response to the high rates charged to industrial customers, many of those customers increasingly pursued these options as a last resort.

This created a dilemma for many utilities and their regulators. Many state commissions began to realize that preserving industrial load -- even if the customer only paid a rate based on marginal costs plus a small contribution to fixed costs -- was better than no industrial load. One by one, state commissions began to phase out the subsidies. This phase out took advantage of a generally favorable cost situation in the industry. Fuel prices were relatively stable or declining, construction budgets were declining because the nuclear construction binge of the '70s and '80s left the industry with excess capacity, and some utilities were actually cutting costs "to prepare for competition." Some commissions held residential rates flat while industrial rates were lowered to capture these declining costs. Because their rates didn't change, few residential customers were aware that their subsidies were being taken away. Perhaps unwittingly, the commissions were preparing ratepayers for "competition" by aligning their regulated rates more appropriately to the utility's actual cost of service.

Question 4: ***In testimony before the Senate Energy and Natural Resources Committee last month, Gregory Conlon of the California Public Utilities Commission told the Committee that enactment of the Telecommunications Act of 1996 delayed the advent of competition in that industry in California, and warned that Congressional enactment of electric restructuring might have the same effect. Do you agree or disagree with this suggestion, and why? If Congress chose to enact retail competition legislation, how should this issue be addressed?***

ELCON Response:

There are too many dissimilarities between "telecom dereg" and "electric dereg" to draw any meaningful conclusions from state compliance with the Telecommunications Act of 1996. If done right, we believe federal legislation should accelerate, not delay, the advent of retail competition in interstate electricity markets. Congress must mandate a "date certain" if all Americans are going to benefit from competition. Simple

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[11]The option to self-generate with cogeneration was greatly increased in 1978 with the enactment of PURPA Title II, especially section 202, which guaranteed interconnection rights, and section 210, which guaranteed backup power at nondiscriminatory rates.

federal guidelines are also necessary to ensure that no state unduly interferes with the operation of interstate electricity markets.

To date, only a few states are making real progress. Most are procrastinating and looking for any excuse to "just go slow." Therefore, a federal mandate is needed.

Question 5: Do you believe prior state action adopting retail competition should be grandfathered?

ELCON Response:

Yes, if the state has adopted retail competition on or before the date certain. However, no prior component of a state action that constitutes a barrier or restraint of interstate commerce in electricity products and services should be grandfathered. Nor should the implementation of customer choice be delayed -- at any state's discretion -- beyond a federally mandated date certain.

Question 6: Recently there has been increased discussion of the need for Congress to enact "reciprocity" requirements barring retail sales of power by parties located in states which have not adopted retail competition to parties in states which have adopted retail competition.

a. Does ELCON have a position on this issue?

b. Which interests would benefit from a federal reciprocity requirement, which would not, and why? Might a federal reciprocity requirement provide an incentive for states with below-market electric generation resources to avoid adopting retail competition policies in order to lock in such power for their own customers?

ELCON Response:

This question highlights the need for a date certain that should be set as soon as possible. ELCON believes that a "reciprocity" provision is unnecessary if this condition is met. The problem only emerges if some states act much quicker than others. All customers will benefit from the removal or reduction of barriers to entry. Any supplier that offers low-cost, quality products or services will also benefit.

Question 7: Please comment on the resolution of stranded cost issues in the retail competition plans adopted in California, Rhode Island, and Pennsyl-

vania. What position, if any, did ELCON take in the relevant state proceedings? Are you generally satisfied with states' resolution of stranded investment issues? How well have states been handling the distinction between costs which were prudently incurred and those which were not? What is your position on state securitization plans with respect to stranded investment?

ELCON Response:

We are not generally pleased with the manner in which this "resolution" was legislated in California and Rhode Island. We do not support any policy purporting to guarantee 100% recovery of such costs from consumers. These costs should be shared. The California law does have provisions that are workably better than the Rhode Island law. The Pennsylvania does not guarantee 100% stranded cost recovery for generating plants.

The Rhode Island law attempts to allow 100% recovery. But it arbitrarily prescribes a stranded cost recovery charge (starting at 2.8¢ per kWh) without any determination of the actual level of stranded costs. An ill-defined true-up mechanism is allowed after three years, but it is not clear how this would work.

California chose not to focus on past prudence, or the "used and usefulness" of stranded assets. Instead, the law focuses on the eligibility of certain stranded costs for recovery. The intent is that once a cost becomes eligible for full recovery (from consumers), it will be fully recovered. However, utilities ultimately are guaranteed only an opportunity to recover those costs. In part, the recovery risk is being shifted to shareholders. Nonetheless, the process will likely prevent consumers from benefitting from competition until after the transition period.

The Pennsylvania law provides Pennsylvania consumers the opportunity to benefit from competition sooner. The law is less prescriptive in the manner in which the stranded cost recovery process is designed. Much is left to the state regulatory commission. The process will be done on a case-by-case, utility-by-utility basis, and any recovery of generating plant stranded costs from consumers must be "just and reasonable." We believe that the Pennsylvania law can result in a fair sharing of stranded costs between each utility and its customers. Attached is a statement by Pennsylvania Commissioner John Hanger which provides an excellent summary and interpretation of the Pennsylvania law and its cost recovery provisions.

ELCON was an early participant in the California "bluebook" proceeding and, together with local industrial groups, advocated a fair and equitable sharing of such

costs. Our position in that proceeding was based on the ELCON document, *Retail Competition in the U.S. Electricity Industry: Eight Principles for Achieving Competitive, Efficient and Equitable Retail Electricity Markets,* dated June 1994. ELCON's position on the stranded cost recovery process is further detailed in the document, "Road Map for the Transition," dated December 22, 1995. Copies of both documents are attached. Local industrial intervention groups participated, and continue to participate, in the Pennsylvania and Rhode Island processes.

ELCON believes that states are ultimately responsible for the resolution of the stranded cost problem. Most of the uneconomic assets or unrealized losses that are considered "strandable" are associated with assets in state-jurisdictional rate bases. State commissions know, or should know, where the skeletons are. It is too early to issue a report card on how well states have been handling the issue. While the earliest activities have not always been fair to consumers (*e.g.,* California, Massachusetts, and Rhode Island), more recent actions in Vermont, New Hampshire, and Pennsylvania are encouraging. We are also beginning to see state legislative initiatives that would limit the recovery from consumers. Clearly, time is a factor. As policymakers and non-industrial consumers become aware of the issue and the risks, they are able to more fairly and actively weigh into the debate. Utilities always have an advantage in moving fast because the technical jargon used to discuss the industry and its problems can be used to obfuscate the real issues. Thus, the early settlements in California and Massachusetts favored the utilities.

With respect to whether a stranded asset was "prudently incurred" or not, it is a matter of case law that that, in and of itself, never guaranteed full recovery. The asset must also remain "used and useful." Neither the California or Rhode Island law requires this test. Texas Commissioner Judy Walsh has articulated this point very well:

> *[Under Texas law] today the utility does not have an absolute right to recover all costs which have been previously found prudent. ... If recovery of these assets is guaranteed at the time of the prudence determination, then the investment is more on the nature of a long-term security, a revenue bond, or a financing transaction. The return on this type of investment would approximate seven percent or some such other bond rate.*

See attached press clipping on Commissioner Walsh and her views.

ELCON believes that securitization may have a limited, but only a limited, role to facilitate the recovery of stranded costs. For example, securitization should be limited to "stranded costs" that are intangible assets, such as regulatory assets. Tangible assets, such as power plants, can be refinanced by traditional means. As proposed in

California, securitization would have only a very narrow application, namely, the financing of an initial rate reduction for residential class customers. Ideally, it should be one of many tools used at the end of the process. Our fear is that this financial instrument can be easily abused and used to bailout high-cost utilities at the expense of consumers. It could easily result in overpayments from customers if the original securitized amount exceeds the actual level of stranded costs. Utilities have every incentive to inflate the initial estimates of their stranded costs to maximize this huge, lump sum payment. Like the refinancing of other bad debt, stretching out the payments over several decades merely creates the illusion of savings. Any opportunity to securitize these costs must not be allowed to discourage mitigation efforts.

The fact that securitization provides utilities with such a huge, up-front cash windfall has been noticed by many utilities. The President of San Diego Gas & Electric Company, Don Felsinger, in describing that company's ambitious proposals for new ventures and acquisitions, said:

> *We are going to have a lot of free cash from stranded-asset recovery ... in the billion dollar range.*

The press clipping containing this quote is attached. What Felsinger has admitted is that San Diego Gas & Electric intends not to use the proceeds of securitization to write off its bonds. If the utility now has this money to freely invest, what was the stranded cost problem in the first place? Finally, IPALCO Enterprises recently published an excellent "white paper" that discusses many of these problems in more detail. A copy of that paper is attached.

Question 8: ***Some proponents of retail competition have argued in favor of federal legislation requiring states to adopt retail competition regimes which include mandatory unbundling of those services currently required by local distribution companies. Does ELCON favor such a policy, why, and if so do you regard this as an essential policy objective?***

ELCON Response:

ELCON strongly advocates the "operational unbundling" of all currently bundled electric services, including those at the distribution level. Each service that is now bundled by the utility should be offered and priced separately. Customers should know what they are paying for distribution services, for transmission services, for generation services, etc. The removal of any and all barriers to entry to each unbundled service -- and the ability to comparison shop for the service -- are essential policy objectives. We have articulated this requirement in both our "Blueprint for

Customer Choice," dated September 13, 1995, and in "Road Map for the Transition," dated December 22, 1995. Copies of each are attached.

While the "wires" associated with local distribution services (and operational control of such facilities) should continue to be regulated as a natural monopoly, all other services such as metering, meter reading, and billing can be outsourced and offered on a fully competitive basis. The interface between the customer and the grid -- for small customers it is the "meter rack" -- should be open to competition in much the same way as the phone company's monopoly over physical interconnection with the phone system was eliminated in 1984. The elimination of that monopoly has spawned an unprecedented explosion of innovations in telecommunications technologies and services, including facsimile machines, answering machines, voice mail, E-mail, cellular phones, pagers, and the World Wide Web. We believe a similar "explosion" is likely in the much larger, deregulated electricity markets.

Another immediate benefit of unbundling is the structural mitigation of cross-subsidization. Cross-subsidization is easier to impose across bundled products and services; it is more difficult to implement after unbundling because each product or service, and its separate price, has greater market visibility. And as long as entry barriers do not exist to new suppliers, the cross-subsidization problem is eventually limited to transactions between regulated and unregulated affiliates. In this limited case, a regulated affiliate would subsidize the costs of one or more unregulated affiliates, passing on those costs to the captive customers of the regulated affiliate. This would result from inadequate regulatory oversight or the lack of regulation (*e.g.*, the existence of a "regulatory gap").

Question 9: What is ELCON's position on the question of whether or not federal legislation is needed to address problems in connection with public power and the federal power marketing agencies? Is transmission a concern? If Congress decides to enact legislation requiring or encouraging adopting retail competition, should any such problems be included in the same bill?

ELCON Response:

ELCON has no formal position on these problems. ELCON has taken the position that the option for public power should be preserved. We feel strongly that the implementation of retail competition should not be delayed until all of these problems are resolved. We are also not yet convinced that federal legislation is necessary to "level the playing field." However, federal legislation may have to deal with certain peripheral issues like allowing the transmission facilities of PMAs and TVA

to be controlled by new independent system operators (ISOs). If other issues need a federal legislative fix, each should be ascertained after retail competition has been introduced. It makes no sense to fix a problem that may only exist in the hypothetical.

Question 10: ***If Congress decides to enact legislation requiring states to adopt retail competition, how can it best avoid constitutional issues relating to the 10th Amendment and "takings" arguments?***

ELCON Response:

ELCON believes federal legislation can be drafted and enacted that avoids either problem. We believe that because Congress has the authority to order retail wheeling in interstate commerce, Congress may order retail access nationally and invite states to participate in this process in a program of "cooperative federalism." The Bumpers bill (S. 237) offers such a scheme of cooperative federalism that should withstand Tenth Amendment scrutiny. Similarly, Congress may adopt legislation like the Schaefer bill (H.R. 655) which requires states to adopt legislation and/or regulations pursuant to Congressional guidance or -- if the state chooses -- allow FERC to develop an appropriate state implementation plan. As to the takings analysis, a federal mandate to enact customer choice, considered under traditional takings jurisprudence and as recognized in a recent case in New York State, will not result in regulatory taking for which compensation must be paid. See attached legal memorandum prepared by ELCON's general counsel, for a more detailed response to this question.

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